

FCC MAIL ROOM

DEC 19 1996

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION

RECEIVED

Washington, D.C. 20554

In the Matter of)

Federal-State Joint Board)
on Universal Service)
_____)

CC Docket No. 96-45

**Comments of California Small Business Association
on the Federal State Joint Board's *Recommended Decision***

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December 18, 1996

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SUMMARY

The California Small Business Association (CSBA) is a nonprofit organization which advocates on behalf of small businesses in California. CSBA regularly polls its members on public policy issues affecting small businesses including telecommunications and receives guidance from its California Small Business Round Table which consists of 40 leading small business owners from across the state. CSBA has 187,000 members, many of whom reside and have small businesses in rural and suburban areas. For this reason, we are vitally concerned that all residential and small business consumers have access to affordable basic and advanced services even in high cost areas.

As the Commission is aware, the *Joint Board's Recommendations* must be measured against the requirements of section 254(d) of the Telecommunications Act of 1996 which provides:

Every telecommunications carrier that provides interstate telecommunications service shall contribute on an equitable and nondiscriminatory basis to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service.

*(Emphasis added.)*¹ In addition, the Joint Board and the Commission must consider the principles set forth in section 254(b).

Unfortunately, the *Joint Board's Recommendations* fail to meet these statutory

¹ Unless otherwise noted, all citations are to the Telecommunications Act of 1996 codified at 47 U.S.C sections 151 *et seq.*

requirements. If adopted, the recommendations will *not* provide a “specific, predictable and sufficient” mechanism to preserve and advance universal service. Instead, they will seriously underfund the cost of providing affordable service in high cost areas by underestimating the cost of providing basic service and overestimating the revenues that carriers will receive in these areas. Nor will the *Joint Board’s Recommendations* require that every telecommunications carrier contribute to the cost of universal service on an “equitable and nondiscriminatory basis.” Instead, some carriers and some consumers (in particular, small business consumers) will bear a disproportionately large share of this cost.

I. The *Joint Board’s Recommendations* Would Underfund Support for High Cost Areas.

The Joint Board recommends, *inter alia*, that support for high cost areas be based on (1) a cost model which assumes the “least-cost, most efficient” technology and (2) a national benchmark of total revenues per line computed by dividing local, discretionary, and access service revenues by the number of loops served. If these recommendations are adopted, the Commission will seriously underfund support in high cost areas.

A. The “Least-Cost, Most Efficient” Technology Standard Will Underestimate the Cost of Serving High Cost Areas.

The “least-cost, most efficient” technology standard is likely to underestimate the cost of providing service in high cost areas. If this “least-cost, most efficient” technology (which is yet to be determined) differs significantly from the technology that carriers are

actually using to provide service in high cost areas, the carriers will be unable to fully recover their cost of service for how ever long it takes to obtain and install the Commission-endorsed technology. In the meantime, these carriers will have to fund the cost of providing universal service in one of two unlawful ways. Either universal service will be funded through implicit subsidies from business lines, toll and other services in violation of section 254(d)'s requirement that the universal service mechanism be "specific, predictable and sufficient." Or universal service will be funded from shareholders funds which would violate section 254(d)'s the requirement that *every* telecommunications carrier contribute to the cost of providing universal service on an "equitable and non-discriminatory basis."

The Commission could avoid these unlawful results in two ways. It could reject the "least-cost, most efficient" standard and base the proxy cost model on the forward-looking, embedded cost of the incumbent local exchange carrier serving the area. Alternatively, the Commission could provide for a transition period which would give carriers serving high cost areas a reasonable period of time to bring their operations into line with the ideal standard.²

B. The Benchmark Overestimates Revenues by Including Discretionary Services.

² The Joint Board has recommended a six-year transition period for carriers meeting the definition of "rural telephone companies." We believe that all carriers whose operations deviate significantly from the yet to be determined "least-cost, most efficient" standard should be allowed a reasonable period of time to conform their operations to the new standard.

The Commission likewise should reject the Joint Board's recommendation to include discretionary services (e.g., call waiting, call forwarding, voice mail and caller ID) in calculating the benchmark. First, discretionary services are *not* among the services supported by the universal service fund. Consequently, the Joint Board's recommendation would require that discretionary services cross-subsidize supported services. This is precisely the type of *non-specific*, implicit subsidy that section 254 and this proceeding were intended to eliminate. See Separate Statement of Commissioner Chong at p. 1 (*emphasis added*) ("One of the key tasks of this Joint Board is to identify all implicit subsidies and to *either remove them or make them explicit.*")

Second, revenues from discretionary services are not a reliable source of funding high cost areas. By their nature, these services are optional (rather than essential) for most consumers. Thus, the amount of revenues derived from these services will depend on factors such as income, employment and prevailing economic conditions in the particular service area.

Rural areas lag far behind urban areas in income and employment. For example, among the 20 most rural counties in California, all have unemployment rates well above the national employment rate. See Exhibit A (comparing unemployment and per capita income for these counties with the nation and California as a whole) attached. Of these 20 counties, nine have unemployment rates that are *more than double* the national rate and one county (Colusa) has an unemployment rate that is *more than triple* the national

unemployment rate. All of the 20 most rural counties in California have a per capita income which is lower than the national per capita income. Six of these counties have a per capita income which is *more than 25 percent below* the national average.³ Similarly, a recent study of nine rural counties in California's Central Valley reported an average unemployment rate of 14.4% for these counties almost *double* the unemployment rate for California and almost *triple* the national unemployment rate. Average household income for these rural counties was \$9,211 (23.5%) below the average household income for California.⁴ In addition, rural areas are often highly dependent on agriculture, natural resources (e.g., timber, mining, commercial fishing, etc.) and recreation or tourism which are seasonal in nature with periods of extremely high unemployment.⁵

Under these circumstances, discretionary services are not a reliable source of revenues to support basic service in high cost areas. The Commission should reject the faulty reasoning that since telephone *penetration* does not vary with household income except for very low income households, revenues from *discretionary services* similarly will not vary with

³ The same holds true for the 20 least densely populated counties in California. See Exhibit B attached. Of these, all have unemployment rates above the national average. Eight of these counties have unemployment rates twice the national rate and two counties have unemployment rates three times the national unemployment rate. All 20 counties have per capita incomes below the national average and seven of these counties have per capita incomes that are more than 25% below the national average.

⁴ See *Economic Map: A Statistical Abstract of the Central Valley*, Central California Futures Institute, California State University at Fresno, 1996, p. 141 and 143.

⁵ See e.g., Trinity County whose economy depends on timber and recreation has an unemployment rate of 14.5% (compared to the national rate of 5.6%) and per capita income 27.3% below the national average.

household income. See Para. 314. Nor should the Commission rely on national averages (which necessarily include more affluent and economically diversified urban and suburban areas) to determine the level of revenues from discretionary services carriers can expect from customers in rural areas. For these reasons, the Joint Board's recommendation to include revenues from discretionary services would violate the requirement that the funding mechanism be "specific, predictable and sufficient."

II. The Commission Should Provide a Reliable Means by Which Carriers May Recover the Cost of Contributing to the Universal Service Fund.

The Joint Board recommends that carriers be required to contribute to the cost of universal service based on gross revenues. Para. 809. However, the Joint Board inexplicably *fails* to recommend *any* method by which carriers could recover such contributions from consumers. Indeed, the Joint Board rejected the proposal that carriers be allowed to recover their contributions through the SLC or a retail end-user surcharge stating "We find that these mechanisms would violate the statutory requirement that carriers, not consumers, finance support mechanisms." Para. 812. The Joint Board also rejected other proposals by which carriers could recover their contributions. *Id.*

The Commission must provide a reliable means by which carriers can recover the cost of contributing to the universal service fund. Contrary to the Joint Board's suggestion, section 254 does not bar such recovery. Indeed, failure to provide an explicit means for carrier's to recover their contributions would violate 254(d)'s requirement that

the funding mechanism be “specific, predictable and sufficient.” It would also make it far more difficult for telecommunications carriers to maintain their networks to provide quality basic service much less make the infrastructure investments needed for advanced service. See sections 254(b)(1), 254(b)(2) and 254(b)(3).

Equally important, adopting the Joint Board’s interpretation regarding the lawfulness of an explicit recovery mechanism would put this Commission on a collision course with a number of states which have adopted explicit surcharges as part of their universal service funding mechanisms. California, for example, recently adopted new universal service rules which require carriers to recover their contributions to that state’s high cost fund through an explicit surcharge on all end users. In so doing, the CPUC concluded that the surcharge conformed to the mandatory requirements of state legislation and specifically rejected the interpretation now embraced by the Joint Board.

D. 96-10-066 at p. 282. The CPUC stated

TURN contends that the language of Section 254(k)(sic) of the Telco Act requires that telecommunications carriers, and not customers, pay into the fund to preserve and advance universal service. We are not persuaded by TURN’s argument that the Telco Act was intended to prevent us from setting up an AEUS [All End User Surcharge] to fund the CHCF-B. *Despite the language in [Section 254(f)], we agree with ICG that it is highly unlikely that Congress intended that carriers only, and not their customers, should contribute to the national fund.* This is especially true since carriers are likely to pass that charge onto its customers. Moreover, carriers who collect the AEUS do not “contribute” to the fund in the sense that they incur administrative expenses. In addition, Section 254(k) of the Telco Act permits the states to adopt regulations pertaining to universal service that are not inconsistent with the FCC’s rules to preserve and advance universal service.

Id. at. pp 184-185. The CPUC further ordered that carriers charge their end users a separate surcharge to recover their contributions to the state's lifeline program. *Id.* at p. 280.

The potential for such a conflict is extremely high. In California, the surcharge for lifeline service is mandated by the Moore Universal Lifeline Telephone Service Act which dates back to 1987. Cal. Public Utilities Code section 879(c). Indeed, the California Legislature considered the surcharge so important to funding universal service that it made it a criminal offense for any telecommunications service provider to fail to collect the surcharge. Cal. Penal Code section 429. In enacting this measure, the Legislature stated

The Legislature further finds and declares that:

- (1) It is in the best interests of the state's telecommunications consumers that the programs and services which are supported by these fees and surcharges be *completely funded* as mandated by the Public Utilities Code.
- (2) Providers of telecommunications services that intentionally do not collect and remit these fees and surcharges thereby gain an *unfair competitive advantage* over the majority of the providers that do collect and remit the moneys in compliance with the mandates of the law.
- (3) The existing provisions of state law are ineffective in ensuring compliance.

Stats. 1990, ch 390, section 1(b) in *Deerings California Statutes Annotated* note to Cal.

Penal Code section 429.

Adoption of the *Joint Board's Recommendations* would directly conflict with California's determination that an explicit surcharge is necessary to fund lifeline service and prevent unfair competition. Nor could the California Public Utilities Commission simply acquiesce to the FCC's determination in this matter. The California Constitution explicitly provides the CPUC has no power "To declare a statute unenforceable, or to refuse to enforce a statute on the basis that federal law or federal regulations prohibit the enforcement of such statute unless an appellate court has made a determination that the enforcement of such statute is prohibited by federal law or federal regulations." Cal. Constitution, Article III, section 3.5.

California is not alone in relying on such surcharges. A recent survey of state commissions reported that seven other states (Arizona, Colorado, Connecticut, Idaho, Kansas, Maine and Utah) use such charges to fund universal service. *State Universal Service Funding Mechanisms: Results of NRRI's Survey*, National Regulatory Research Institute, May 1996, p. 22. The Joint Board's recommendation would wreak havoc on these state programs and give rise to another legal confrontation between state and federal regulators over the proper interpretation of the Telecommunications Act.⁶

⁶ See, for example, *Iowa Utilities Board, et al. v. FCC*, 1996 U.S.App. LEXIS 27953 where the Eight Circuit expressed "serious doubts" regarding the Commission's interpretation of the Act concluding that the states were likely to prevail in their challenge to the pricing portions of the Commission's First Report and Order in CC Docket No. 96-98.

For these reasons, the Commission should adopt a specific, predictable and sufficient mechanism to allow carriers to recover their contributions to support universal service. This should include *all* contributions that carriers are required to make under section 254, whether they are to support high cost areas, discounts for schools, libraries and health care providers or low income consumers.

III. The Commission Should Provide Support for Second Lines.

The Joint Board recommends that support in high cost areas should be limited to services (1) provided on a single connection to a subscriber's principal residence and (2) to single-connection businesses. The Commission should extend support to second lines.

Affordable second lines are essential to the development of home-based businesses, telecommuting, home-to-school connectivity, expanded Internet access for students and businesses. In short, they play an important social and economic role in high cost areas.

Adopting the Joint Board's recommendation would threaten the affordability and availability of second lines in high cost areas. For example, in its comments to the CPUC, GTE of California, the state's second largest local exchange carrier, stated that if second lines are not a part of the definition of universal service: (1) no Carrier of Last Resort should be required to provide second line service against its will and (2) the price of second lines should be deregulated or at least raised to a proper measure of cost.

Comments of GTE California Incorporated (U 1002 C) on Proposed Decision of ALJ

Wong in R.95-01-020 / I. 95-01-021, August 26, 1996, at p. 17. In addition, to the extent that the Commission fails to provide sufficient funding for primary lines, local exchange carriers will have to increase their rates for second lines to collect this shortfall.

IV. The *Joint Board's Recommendations* Would Have Serious Negative Consequences for Rural and Suburban Communities.

Unless the *Joint Board's Recommendations* are modified to correct these problems, they will result in a fund which will not support the level of service needed in high cost areas. This, in turn, will have serious negative consequences for rural and suburban consumers.

A. There will be no facilities-based competition.

Because the size of the fund will be unrealistically low, there will be no economic incentive for new local service providers to build new facilities to compete with those of existing telephone companies. Facilities-based competition will continue to be concentrated only in high traffic commercial districts. In rural and suburban areas, competition will be limited to resale of existing services. Consequently, in these areas, consumers will not receive the far-reaching benefits of competition in the design, construction and operation of physical networks.⁷ In this regard, the *Joint Board's Recommendations* are contrary to the principle that

⁷ Nor will local governments and local businesses realize the substantial economic benefits from construction and maintenance of new network facilities in their communities.

Consumers in all regions of the Nation, including ... those in rural, insular, and high cost areas, should have access to telecommunications and information services, including local exchange services and advanced telecommunications and information services that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

Section 254(b)(3).

B. Consumers in high cost areas will be served by outdated technology.

By failing to establish a sufficient and reliable means of funding the cost of universal service, the *Joint Board's Recommendations* ensure that existing telephone companies will not have either the financial ability or incentive to modernize their networks to provide basic and advanced services needed by residential and business customers in rural and suburban areas. Thus, *Joint Board's Recommendations* violate section 254(b)(1) ("Quality service should be available at just, reasonable and affordable rates") and section 254(b)(2) ("Access to advanced telecommunications and information services should be provided in all regions of the Nation") as well as section 254(b)(3).

C. Rural and suburban customers will face substantially higher rates for basic telephone service.

The *Joint Board's Recommendations* will mean that rural and suburban customers will face higher rates for basic telephone service. By underestimating costs and overestimating revenues, the *Joint Board's Recommendations* will create financial pressure on existing telephone companies to raise their rates to cover the cost of providing universal service. In addition, residential and business consumers are likely to

see substantially higher rates for second lines which will receive no support even in the highest cost areas. Higher rates will be a significant obstacle to expanded Internet access, home-to-school connectivity, the development of home-based businesses, telecommuting, the establishment and expansion of small businesses and economic development in these areas.

D. Meanwhile, consumers will pay more than they should for long distance services.

Too often, small business consumers are the last to benefit from competition but the first to pay the price. In this case, whether it is through an explicit surcharge or implicit subsidies, small businesses will bear a large share of the cost of the new universal service program. Small business consumers would benefit from competition if the Commission expedited the process of allowing the former Bell Operating Companies (BOCs) to enter the inter-LATA long distance markets. Currently, AT&T, MCI and Sprint are protected from direct, head-to-head competition from BOCs in these lucrative markets. As a result, consumers (especially small business consumers) are paying more than they should for long distance services. Rather than continuing to protect the profits of long distance companies, the Commission should allow BOCs to enter inter-LATA markets.

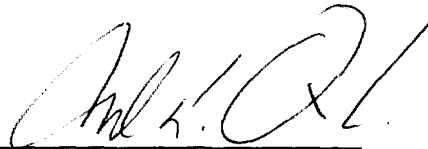
Conclusion

For the reasons set forth above, CSBA requests that this Commission (1) reject the

Joint Board's Recommendations which understate costs and overstate revenues in determining the level of support for high cost areas, (2) establish a reliable means by which carriers may recover the cost of contributing to support universal service, (3) extend support to second lines, and (4) allow BOCs to compete in inter-LATA markets on an expedited basis.

Date: December 18, 1996

By



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Areas Ranked By % Rural

<u>Area</u>	<u>% Rural Population</u> <u>1990</u>	<u>Unemployment</u> <u>Rate - % 1995</u>	<u>Income Per Capita</u> <u>1994</u>
United States	24.8%	5.6%	\$ 21,699
California	7.4%	7.8%	\$ 22,345
<u>County - 20 Most Rural</u>			
Alpine	100.0%	10.2%	\$ 21,169
Mariposa	100.0%	9.4%	\$ 17,482
Sierra	100.0%	9.4%	\$ 18,318
Calaveras	88.2%	11.1%	\$ 16,715
Plumas	78.4%	13.3%	\$ 18,722
Lassen	73.6%	11.0%	\$ 15,699
Tuolumne	73.1%	10.8%	\$ 17,496
Colusa	69.7%	19.7%	\$ 20,953
Siskiyou	69.1%	14.5%	\$ 17,118
Mendocino	68.0%	9.6%	\$ 18,790
Nevada	68.0%	7.3%	\$ 19,704
Modoc	66.6%	12.9%	\$ 15,588
Amador	66.5%	8.2%	\$ 17,161
Del Norte	64.9%	12.3%	\$ 13,818
Tehama	63.3%	11.0%	\$ 14,477
Lake	62.2%	11.7%	\$ 17,870
El Dorado	56.0%	7.0%	\$ 21,287
Glenn	55.5%	15.2%	\$ 15,599
Mono	54.8%	10.9%	\$ 20,335
Trinity	54.5%	14.5%	\$ 15,957

Sources

% Rural Population

U.S.: 1996 US Statistical Abstract, Table 44, p.43.

Calif: 1990 Census, STF3A

Unemployment

U.S.: 1996 US Statistical Abstract, Table 614, p. 393.

Calif: California Statistical Abstract 1996, Table C-2.

Income Per Capita

U.S.: 1996 US Statistical Abstract, Table 699, p. 453.

Calif: California Statistical Abstract 1996, Table D-7.

Areas Ranked By Population Per Square Mile

<u>Area</u>	<u>Population Per Sq. Mile, 1995</u>	<u>Unemployment Rate - %, 1995</u>	<u>Income Per Capita 1994</u>
United States	74.3	5.6% \$	21,699
California	205.6	7.8% \$	22,345
<u>County - 20 With Least Population Density</u>			
Alpine	1.6	10.2% \$	21,169
Inyo	1.8	9.3% \$	19,347
Modoc	2.5	12.9% \$	15,588
Mono	3.5	10.9% \$	20,335
Sierra	3.6	9.4% \$	18,318
Trinity	4.2	14.5% \$	15,957
Lassen	6.3	11.0% \$	15,899
Siskiyou	7.1	14.5% \$	17,118
Plumas	8.0	13.3% \$	18,722
Mariposa	11.0	9.4% \$	17,482
Colusa	15.5	19.7% \$	20,953
Tehama	18.4	11.0% \$	14,477
Glenn	20.2	15.2% \$	15,589
Tuolumne	23.0	10.8% \$	17,496
Mendocino	24.0	9.6% \$	18,790
Del Norte	27.4	12.3% \$	13,818
San Benito	30.7	13.5% \$	17,263
Imperial	32.9	28.8% \$	14,302
Humboldt	34.8	8.3% \$	18,105
Calaveras	36.2	11.1% \$	16,715

Sources

Population Per Sq. Mile - 1995

U.S.: 1996 US Statistical Abstract, Table 28, p.29.

Calif: California Statistical Abstract 1996, Tables A-1 and B-3.

Unemployment Rate - 1995

U.S.: 1996 US Statistical Abstract, Table 614, p. 393.

Calif: California Statistical Abstract 1996, Table C-2.

Income Per Capita - 1994

U.S.: 1996 US Statistical Abstract, Table 699, p. 453.

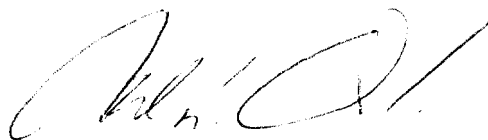
Calif: California Statistical Abstract 1996, Table D-7.

Certificate of Service

Case: In the Matter of Federal State Joint Board on Universal Service (CC Docket No. 96-45).

I, Carl K. Oshiro hereby certify that I have upon this day served a copy of the attached *Comments of California Small Business Association on the Federal State Joint Board Recommended Decision* by mailing a copy via first class mail upon all persons and entities on the service list for the above proceeding. (A list of the names and of the persons and entities served is attached to the original certificate filed with the Commission.)

Dated at San Francisco, California on December 18, 1996.



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CC Docket No. 96-45**

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